



Australian Government

Takeovers Panel

**Reasons for Decision
Wollongong Coal Limited
[2014] ATP 21**

Catchwords:

Decline to commence proceedings - disclosure - dispersion strategy - effect on control - need for funds - rights issue - accelerated offer - delay in application - control effect - legal basis - debt for shares - shortfall discretion - artifice

Corporations Act 2001 (Cth), sections 602, 657A

Brierley Investments Ltd v ASIC (1997) 24 ACSR 629 Elders IXL Ltd v NCSC [1987] VR 1

Guidance Note 17 Rights Issues

Altius Mining Limited [2012] ATP 17, Real Estate Capital Partners USA Property Trust [2012] ATP 6, Powerlan Limited [2010] ATP 2, Multiplex Prime Property Fund 03 [2009] ATP 22, Redflex Holdings Limited [2009] ATP 17, Gloucester Coal Limited 01R(a) and (b) [2009] ATP 9, Gloucester Coal Limited 01 [2009] ATP 6, Dromana Estate Limited [2006] ATP 4, Village Roadshow Limited 02 [2004] ATP 12

Interim order	IO undertaking	Conduct	Declaration	Final order	Undertaking
NO	NO	NO	NO	NO	NO

INTRODUCTION

1. The Panel, Karen Evans-Cullen, Ron Malek and Vickki McFadden (sitting President), declined to conduct proceedings on an application by Gujarat NRE India Pty Ltd (Controller Appointed) in relation to the affairs of Wollongong Coal Limited. The application concerned whether, having conducted 4 rights issues recently, a 19:20 rights issue would have a substantial control effect. The Panel considered that there was no reasonable prospect that it would declare the circumstances unacceptable.

2. In these reasons, the following definitions apply.

- Gujarat Gujarat NRE India Pty Ltd (Controller Appointed)
- Jindal Jindal Steel and Power Limited and its subsidiaries: Jindal Steel & Power (Mauritius) Limited and Jindal Steel & Power (Australia) Pty Limited
- rights issue The accelerated, pro-rata, renounceable 19:20 entitlement offer at an issue price of \$0.018 per new share announced on 4 November 2014 by WLC to raise up to approximately \$66.68 million.
- WLC Wollongong Coal Limited

FACTS

3. Wollongong Coal Limited is an ASX listed company (ASX code: WLC). It carries on the business of mining and producing coal for sale and export at Wollongong.

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4. The Gujarat Group, which consists of Gujarat NRE Coke Limited (an Indian listed company) and its subsidiaries including the applicant, holds approximately 6.94% of Wollongong.
5. Jindal (an Indian listed company) is an international steel and power company. It has funded WLC and holds debt. In May 2012, Jindal became a substantial holder in WLC following purchases and a placement. In 2013, Jindal made a bid for WLC. On 16 October 2013 shareholders approved Jindal receiving a placement and top-up, which, when the shares were issued in November 2013, took its interest to 53.63%. Since acquiring a majority controlling stake in, and management control of, WLC most of WLC's coal production has been sold to Jindal. Previously WLC was controlled and managed by Gujarat's parent entity, Gujarat NRE Coke Limited, and most of WLC's coal production was sold to it.
6. WLC has experienced recurrent difficulties concerning liquidity and working capital. On 31 October 2013, Jindal provide a bridging loan of \$50 million for WLC, which was increased to \$75 million in November 2014. It has also provided a letter of support.
7. WLC has conducted four previous rights issues in recent times, as follows:
 - (a) in November 2013, an accelerated non-renounceable rights issue at 8 cents per share to raise \$108 million (\$58 million raised)
 - (b) in January/February 2014, an accelerated non-renounceable rights at 8 cents per share issue to raise \$40 million (\$26.4 million raised)
 - (c) in April 2014, an accelerated pro-rata renounceable rights issue at 7.5 cents per share to raise \$42.84 million (\$29.36 million raised) and
 - (d) in May 2014, an accelerated non-renounceable rights issue at 6 cents per share to raise \$30.3 million (\$21.76 million raised).¹
8. The previous rights issues had practically no take up by shareholders other than Jindal, which has led to Jindal increasing its voting power from 53.63% to 74.39%.
9. On 4 November 2014, WLC announced the rights issue at 1.8 cents per share. It is not underwritten.
10. The rights issue includes a separate offer to all shareholders (other than Jindal and the directors) to participate in any shortfall. The prospectus discloses that the directors "*will issue any Shortfall Shares at their discretion only by majority decision of the Board*".
11. If no shareholders other than Jindal take up their entitlements under the rights issue, Jindal will increase its interest from 74.39% to 84.99%.

APPLICATION

Declaration sought

12. By application dated 20 November 2014, Gujarat sought a declaration of unacceptable circumstances. It submitted that the rights issue is the fifth one recently

¹ all figures approximate

undertaken and part of a strategy to deliver WLC to Jindal without Jindal paying a control premium. It submitted that the rights issue was not justified given WLC's financial circumstances.

13. It submitted that the effect of the circumstances was an unnecessary, significant impact on control of WLC and a takeover by stealth. It also submitted that the directors had not taken reasonable steps to minimise the potential impact on the control of WLC.

Interim orders sought

14. Gujarat sought interim orders to the effect that Jindal be prevented from acquiring further shares or increasing their voting power, be prevented from disposing of or transferring any shares, and be prevented from exercising any voting rights attaching to shares in WLC.

Final orders sought

15. Gujarat sought final orders that:
 - (a) the rights issue be cancelled or prevented from proceeding
 - (b) applications be considered void and application money returned
 - (c) Jindal be restrained from proceeding with compulsory acquisition or otherwise acquiring any further relevant interest in WLC and
 - (d) WLC be restrained from buying back unmarketable parcels of shares in WLC.

DISCUSSION

16. The applicant, Gujarat, submitted that there had been a takeover by Jindal, followed by a placement with item 7 approval, followed by board changes, followed by the series of rights issues. It submitted that:

The circumstances in this case, where the rights issue is almost exclusively for the purpose of paying back monies outstanding under the Jindal Credit Facility by converting debt to equity, make Jindal a de facto underwriter of the rights issue. It is our submission therefore, that the Rights Issue being a deliberate ploy to give control to Jindal is an abuse of the [sic] s 611 item 10.

17. WLC, in a preliminary submission, submitted that Jindal already had control and there was no control issue arising under the rights issue. It submitted that the application had no legal basis. It submitted that Jindal acquired effective control of WLC with the approval of non-Jindal shareholders (including Gujarat Group) in 2013.
18. We do not agree that the application has no legal basis. We do not accept the submission that there is no control issue. There is an increase in control likely to come about by reason of the rights issue, in that Jindal is likely to increase its interest

from 74.39% to around 84.99% after the offer closes.² Jindal has accepted the accelerated offer part of the rights issue. We note that Jindal was the only institution receiving the accelerated offer.³ WLC submitted that the rights issue will not take Jindal above the 90% threshold that would allow compulsory acquisition. The increase does not take Jindal to the level at which it can undertake compulsory acquisition, but it is the acquisition of a substantial interest and, in our opinion, has a potential control effect.

19. The Panel may make a declaration if it appears that the circumstances are unacceptable having regard to the effect the Panel is satisfied they have had, are having, will have or are likely to have on the acquisition or proposed acquisition of a substantial interest.⁴ Given that it appears unlikely that all shareholders will take up their rights, Jindal will, in that event, acquire a substantial interest having taken up the accelerated part of the rights issue.
20. Alternatively, the Panel may make a declaration having regard to the effect the Panel is satisfied the circumstances will have or are likely to have on the control or potential control of the company.⁵ As the Panel in *Gloucester Coal* said:
*Section 657A empowers the Panel to consider whether a transaction that has an effect on the control of a company, or on the acquisition of a substantial interest in a company, is unacceptable having regard to the policy of Chapter 6, even if it does not breach any provision of Chapter 6.*⁶
21. In *Village Roadshow 02*, although concerned with a buy-back proposal, the Panel said:
*... The takeovers code is consistently concerned with fine gradations of control, and does not treat control as an absolute concept. Chapter 6 regulates acquisitions of shares conferring voting power across the whole of the range from 20% to 90% voting power. Chapter 6C requires disclosure of voting power across the whole of the range from 5% to 100% voting power, in increments of 1%. Panels have consistently explained the relationship between unacceptable circumstances and control in terms of increments of control, as have the Courts.*⁷
22. Accordingly, we think that the application has a legal basis.
23. WLC also submitted that it had implemented significant protections including that the rights issue was renounceable, that Jindal was not underwriting it, that eligible shareholders could apply for additional shares and that the shortfall offer would remain open for 3 months. It also submitted that it was carrying out the rights issue because of “*an immediate and compelling need for funds*”, which, it submitted, was in

² *Post script*: WLC announced on 5 December 2014 that it had raised \$50,737,000 out of a possible \$66,667,000.

³ Paragraph 5.2 of the Prospectus dated 4 November 2014 says: “*The Company will conduct the institutional component of the Offer made to the Jindal Group (Institutional Entitlement Offer) during the period set out in the timetable.*”

⁴ Section 657A(2)(a)(ii)

⁵ Section 657A(2)(a)(i)

⁶ *Gloucester Coal Limited 01* [2009] ATP 6 at [30], adopted in *Gloucester Coal Limited 01R(a) and (b)* [2009] ATP 9 at [23]

⁷ *Village Roadshow Limited 02* [2004] ATP 12 at [34]

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part contributed to by a member of the Gujarat Group failing to pay for coal that had been supplied to it.⁸

24. Guidance Note 17 makes it clear that in considering whether unacceptable circumstances exist, the Panel considers whether, if there is potential for a rights issue to affect control, the directors have carefully considered all reasonably available options to mitigate that effect. The Panel considers, among other things, whether the control effect exceeds what is reasonably necessary for the fundraising purpose.⁹ The Panel is likely to accept the directors' decision on need for funds, if the decision appears reasonable and supported and the applicant cannot point to something warranting deeper inquiry. A large issue may require the company to demonstrate more clearly the need for funds.¹⁰
25. It appears from the material that there is a need for funds. WLC submitted that it is in severe financial difficulty, has no current source of income and has been the subject of several recent winding up applications. According to the March 2014 audited financial report, the company's net liabilities were in the order of \$458 million. A capital raising of \$66 million is questionable as a fund raising saviour. This is perhaps more acute given that the rights issue appears to be repaying a non-current borrowing. This caused us to have reservations about whether the rights issue was proposed because of the need for funds.
26. On the other hand, if the capital raising had been undertaken to repay a debt to a third party there would be little to enquire about. It does not appear to us that there is any reason (and none was given in the application) that we should conduct proceedings just because the debt is owed to Jindal.
27. The question for us is whether the capital raising is so flawed as to give rise to unacceptable circumstances. On balance, we do not think so. While there are potentially some issues raised regarding underwriting, shortfall and need for funds, the rights issue complies in most respects with the Panel's guidelines on minimising control impact.
28. The structure of the rights issue includes an accelerated part, in circumstances where the only institution to receive the accelerated offer is Jindal and it is exchanging debt for the shares it receives. We do not think this is *de facto* underwriting, as the applicant submitted. We view the accelerated part as similar to a statement of intention by the major shareholder about taking up its rights. WLC submitted that the shares had already been issued to Jindal and "*As a consequence, the Application (indicating the purported unacceptable circumstances are continuing) and the corresponding interim and final orders (that no shares be issued to Jindal) are flawed and unable to be granted*". We would not feel ourselves bound, despite the argument to the contrary by WLC, by the fact that the accelerated part had been completed if the rights issue was otherwise unacceptable.

⁸ The preliminary submission suggested that this latter point supported an argument that the application had been made to reduce WLC's ability to fund actions against that member

⁹ Guidance Note *Rights Issues* 17 at [5]

¹⁰ Guidance Note 17 *Rights Issues* at [7] and [14]. See also *Multiplex Prime Property Fund 03* [2009] ATP 22, at [47]

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29. The rights issue is renounceable. This helps reduce flow-through to an underwriter (although there is none here) and also helps pass the rights to persons more likely to want to take them up. This helps minimize the potential control effect. We note however that WLC shares were thinly traded between September and November 2014 at prices between 2.5 cents in September and 1.6 cents in November. The rights issue price is 1.8 cents. Gujarat submitted that *"This rights issue is an example of a renounceable offer that is, in effect non renounceable due to the virtual non-existent market for rights."*
30. In a thinly traded stock, as here, this difficulty always faces a company undertaking a renounceable rights issue. We do not think the rights issue price is so far removed from the recent trading price that we should ignore this feature of the rights issue entirely.
31. Secondly, Jindal is not underwriting the Rights Issue and is only taking up its entitlement. Against this, there is no underwriting. While the lack of underwriting is likely to concentrate control in Jindal if other shareholders do not take up their rights, we recognise that *"For many companies, a related party or major shareholder is the only realistic source of underwriting (sub-underwriting)."*¹¹ And this is likely to be the position here. Jindal at least is not underwriting the offer. Had it done so, it may have resulted in an increase in its interest to above the 90% level, and our position may have been different.
32. Thirdly, eligible shareholders are able to apply for shares in addition to their entitlement, but neither Jindal nor any related party of any director of WLC is able to apply for additional shares. The offer of the shortfall shares will remain open for 3 months following the closing date of the Rights Issue. There is some protection in this feature of the rights issue from a control perspective, particularly for any shareholder, such as Gujarat, concerned about the increasing level of control in Jindal.
33. WLC appears to have taken reasonable steps to minimise the potential control impact of the rights issue, except in respect of the shortfall. In terms of the shortfall offer, the prospectus states that *"the Directors will issue any Shortfall Shares at their discretion only by a majority decision of the Board. Priority will be given to Eligible Shareholders who are not related parties to the Company. Neither the Jindal Group nor any party related to any Director will be able to apply for shares under the Shortfall Offer."*
34. The Panel has regularly rejected an open-ended discretion regarding the placement of shortfall shares.¹² But for the need for funds, the discretion here sits close to the margin. Indeed, we would be concerned if the discretion of the directors to allocate shortfall shares to applicants, particularly existing shareholders, was exercised in a way that did not facilitate an appropriate dispersion strategy. In this respect, WLC should note the method for allocating shortfall required in, for example, *Real Estate*

¹¹ GN 17 *Rights Issues* at [21]

¹² *Dromana Estate Limited* [2006] ATP 4 at [30]-[32], *Redflex Holdings Limited* [2009] ATP 17 at [28], *Powerlan Limited* [2010] ATP 2 at [42]-[43], *Altius Mining Limited* [2012] ATP 17 at [30]

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Capital Partners.¹³ We have no reason to believe that WLC will not allocate shortfall appropriately, but if it does not then a fresh application can be made.

35. Overall, we considered the disclosure in the prospectus to be appropriate.
36. Gujarat submitted that “*there is a well-established precedent for a declaration of unacceptable circumstances where a rights issue is really an artifice for a major shareholder seeking to wrest further control through unacceptable underwriting arrangements or similar (for example Anaconda Nickel Ltd 02-05; Phosphate Resources Ltd [2003] ATP 03; Lachlan Farming Ltd [2004] ATP 31; Rivkin Financial Services 02 [2005] ATP 1).*”
37. We are not satisfied that the rights issue here is an artifice. It is different to the cases cited by the applicant. In *Anaconda*, the rights issue was a significantly dilutive 14:1 issue. In *Phosphate Resources*, the company proposed a buy-back then, shortly after, a rights issue which would take the underwriting shareholder from below 20% to above 30%. In *Lachlan Farming* the rights issue could have taken the partial underwriting shareholder from 1.97% to 46.7%.¹⁴ In *Rivkin* there was a contest for control that the rights issue could have an effect on, no need for the funds and unacceptable underwriting terms.
38. One other factor influenced our decision not to conduct proceedings. We note the preliminary submission of WLC that “*the Application is opportunistic, vexatious, [and] for a collateral purpose.*” While we were unwilling to investigate this further, and so make no comment on the correctness of the submission, the application did appear to have some other purpose than simply a concern by a shareholder. Gujarat had control of this company and by shareholders’ agreement it was passed to Jindal. The parties clearly have a relationship, including coal supply arrangements over which there appears to be some dispute. The preliminary submission suggests that a member of the Gujarat Group is indebted to WLC. Gujarat has waited until the fifth rights issue to complain. The rights issue does not appear to be materially different to the last four in structure, nor is it significantly larger. Gujarat was aware that the rights issue was accelerated but waited more than 2 weeks before making its application. The rights issue was announced on 4 November 2014 and the application not made until 20 November 2014.
39. Lastly, we note that the structure of the rights issue is such that there is no reason why Gujarat (and other shareholders) cannot protect their current interest, and prevent the potential dilution of their interests that is the subject of the application, by taking up their rights and, indeed, applying for shortfall shares.

DECISION

40. For the reasons above, we do not consider that there is any reasonable prospect that we would make a declaration of unacceptable circumstances. Accordingly, we have decided not to conduct proceedings in relation to the application under regulation 20 of the *Australian Securities and Investments Commission Regulations 2001 (Cth)*.

¹³ *Real Estate Capital Partners USA Property Trust* [2012] ATP 6

¹⁴ The Panel declined to commence proceedings

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Orders

41. Given that we have decided not to conduct proceedings, we do not (and do not need to) consider whether to make an interim order.

Vicki McFadden

President of the sitting Panel

Decision dated 26 November 2014

Reasons published 12 December 2014

Advisers

Party	Advisers
Gujarat NRE India Pty Ltd (Controller Appointed)	Piper Alderman
Wollongong Coal Limited	HopgoodGanim